

STELLENT INC
Form 10-K
June 14, 2006

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended March 31, 2006

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number 0-19817

Stellent, Inc.

(Exact name of registrant as specified in its charter)

Minnesota
(State or other jurisdiction of
incorporation or organization)

41-1652566
(I.R.S. Employer
Identification No.)

7500 Flying Cloud Drive, Suite 500

Eden Prairie, MN 55344

(Address of principal executive offices and zip code)

(952) 903-2000

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act: Preferred Share

Purchase Rights; Common Stock, par value \$.01 per share

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Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act (Check one)

Large Accelerated Filer Accelerated Filer Non-Accelerated Filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

The aggregate market value of the registrant's common stock held by non-affiliates of the registrant as of September 30, 2005 was approximately \$221,109,000 based on the closing sale price for the registrant's common stock on that date as reported by The NASDAQ Stock Market. For purposes of determining such aggregate market value, all officers and directors of the registrant are considered to be affiliates of the registrant, as well as shareholders holding 10% or more of the outstanding common stock as reflected on Schedules 13D or 13G filed with the registrant. This number is provided only for the purpose of this report on Form 10-K and does not represent an admission by either the registrant or any such person as to the status of such person.

As of June 2, 2006, the registrant had approximately 29,555,000 shares of common stock issued and outstanding.

STELLENT, INC.

FORM 10-K

For the fiscal year ended March 31, 2006

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DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive Proxy Statement for the annual meeting of Shareholders to be held on August 1, 2006 are incorporated by reference in Part III of this Annual Report on Form 10-K. (The Compensation Committee Report and the stock performance graph contained in the registrant's Proxy Statement are expressly not incorporated by reference in this Annual Report on Form 10-K). The Proxy Statement will be filed within 120 days after the end of the fiscal year ended March 31, 2006.

Item 1. *Business*

Forward-Looking Statements

The information presented in this Annual Report on Form 10-K under the headings Item 1. Business, Item 2. Properties, Item 3. Legal Proceedings, Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation and Item 7A. Quantitative and Qualitative Disclosures About Market Risk contain forward-looking statements within the meaning of the safe harbor provisions of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Such forward-looking statements are based on the beliefs of our company's management as well as on assumptions made by, and information currently available to, us at the time such statements were made. When used in the Annual Report on Form 10-K, the words approximate, anticipate, believe, estimate, expect, intend, and similar expressions, as they relate to us, are intended to identify such forward-looking statements. Although we believe these statements are reasonable, such statements are subject to risks and uncertainties, including those discussed under Item 1A. Risk Factors of this Annual Report on Form 10-K, that could cause actual results to differ materially from those projected. Because actual results may differ, readers are cautioned not to place undue reliance on these forward-looking statements.

OVERVIEW

In 1997, we launched one of the first software product suites on the market that was fully developed and created expressly for Web-based content and document management. At the time, content management today considered a critical component of an organization's communication and information technology (IT) infrastructure was an emerging technology used to help companies easily and quickly share information with employees, partners, customers and prospects using the World Wide Web.

Currently, our suite of software solutions help customers worldwide solve business problems related to efficiently creating, managing, sharing and archiving critical information.

We help our customers optimize the use of our software products by providing them with value-based consulting services related to their content management needs. We also provide our customers with a range of product support programs that allow them to select maintenance and support services that are appropriate for their business.

PRODUCTS AND SERVICES

Stellent's products and services consist of content management, filtering and conversion software products; electronic content management consulting services; and post-contract software maintenance and support.

Content Management, Filtering and Conversion Software

Universal Content Management is Stellent's primary software product, consisting of a unified architecture and product which power multiple applications. These applications help organizations manage their business information such as records, legal documents such as contracts, business documents, presentations, Web content and graphics via the Web, from the time it's created to the time it's archived

or disposed of, so employees, customers, partners and investors can more easily find, access and re-use that information. With Stellent software, customers can increase employee productivity, reduce expenses and improve company-wide collaboration and communication.

Our Universal Content Management software addresses the key elements of content management document management and imaging, Web content management, digital asset management, records and retention management, and collaboration from a unified architecture, enabling customers to fully leverage their content management investment across the organization. We believe our tightly integrated products allow companies to implement content management-based applications using fewer products and consulting services than other content management offerings, which can lead to a lower total cost of ownership.

Both technical and non-technical users find using the Stellent system easy. Users can submit, or contribute, business content such as a word processing document, spreadsheet, CAD file or image to the Stellent system, and the Stellent technology automatically converts the file to a format that can be viewed on a Web site without needing the software application that created the file. This automatic conversion capability enables even non-technical users to easily publish information to a site, such as an employee portal or partner extranet, so the information can be shared with other users.

Our Universal Content Management software is comprised primarily of Stellent Content Server a data repository that provides a core set of content services to help ensure users can access only the most current information as appropriate to their role or permissions the following five key content management application modules:

- *Web Content Management:* Enables organizations to create web content, and manage and publish Web sites.
- *Document Management and Imaging:* Provides Web-based management, collaboration and access to business information created in common office software applications or created as paper documents which are then converted into electronic images.
- *Digital Asset Management:* Enables digital assets such as photos, graphics, audio clips and video clips to be searched, accessed, viewed, managed, distributed and re-purposed via the Web.
- *Records and Retention Management:* Provides a Web-based method for managing business records and creating rules such as expiration, archiving and deletion regarding how long content needs to be retained and what actions to take regarding the content.
- *Collaboration Management:* Enables the creation of a project or team space for sharing documents, schedules and discussions among a team via the Web.

Stellent also offers end-user and OEM customers the content filtering and conversion components of its Universal Content Management software. These technologies make information created in more than 390 common office software applications more accessible to the business users who need it. Since business information is often difficult to access without the native software application in which it was created, Stellent's technologies convert files into any one of 11 common output formats, empowering users to locate and view information without needing the software application that created the file. Other technology companies embed these technologies in their own solutions to enable them to extract text and metadata and provide a high-fidelity view of file contents.

Consulting Services

Our consulting services group is focused on delivering value-based content management solutions to our customers. Our consulting services professionals employ a combination of business analysis, enterprise architecture, application analysis, installation, configuration, development and integration skills with

experience-based project methodology and management knowledge to facilitate the rollout of content management solutions at all levels of a customer's organization. Available on a worldwide basis, we act as a business partner to our customers by providing a broad spectrum of services including:

- Technical architecture analysis and needs assessment, such as software, security and metadata analysis
- Solutions development and deployment strategies
- Software installation and configuration
- Custom application development
- Third party product integration
- Project management
- Knowledge transfer

These services can be offered in conjunction with our software products to new customers, or on a stand alone basis to our existing customers to assist them in driving additional content management solutions across their enterprises. These services are sold in conjunction with our software products and are offered for fees, the amount of which depends on the nature and scope of the project.

Product Support

We offer several product support programs that allow customers to select the offering(s) that best satisfies their maintenance and support requirements. From the initial installation and configuration of Stellent to the point of application deployment, our product support resources offer customer service through quick response time, trouble-shooting and the delivery of complete and comprehensive technical solutions. Customers may access product support resources on a worldwide basis for assistance during the customer's normal business hours. Additional support offerings are available which supplement the customer's product support requirements.

Product support offerings are renewable on an annual basis and are typically priced as a percentage of the product license fees or percentage of product list price.

MARKETS AND CUSTOMERS

As of March 31, 2006, approximately 4,153 end-user content management, viewing and conversion customers and 549 OEM customers had selected Stellent solutions to power their content-centric business applications. No single customer accounted for ten percent or more of our total revenues in fiscal year 2006.

Customers primarily use our products as follows:

- *Enterprise Content Management:* Enterprise content management (ECM) is an infrastructure for all content-based applications such as public-facing Web sites, corporate intranets, dealer and partner extranets, human resource portals, customer service Web sites, marketing brand management, and accounts payable imaging within an enterprise, allowing organizations to strategically select, deploy and maintain an effective, efficient knowledge platform within their organizations. Often times, the ability to provide an ECM infrastructure is a requirement in line-of-business transactions as companies look ahead to other upcoming content management needs.

Multi-Site Management: Multi-site management refers to a content management infrastructure for creating and managing multiple, distributed Web properties such as public Web sites, intranets, extranets and portals. Stellent's second-generation, multi-site management solution offers a rapidly deployable product, allowing companies to easily launch and maintain multiple internal or external sites while preserving appropriate corporate branding.

- *Governance, Risk and Compliance:* The increasingly expanded visibility of various compliance requirements most notably Sarbanes-Oxley continues to be a significant factor in technology infrastructure and application purchasing decisions. Compliance solutions powered by content management technologies both as platforms to support multiple compliance initiatives across organizations and specific solutions to individual regulatory challenges assist organizations in their compliance processes by automating the capture, management, retention and disposition of critical documentation for processes, objectives and risks, as well as the long-term management of the physical and electronic documentary evidence of regulatory compliance.
- *Enterprise Records and Retention Management:* The tremendous amount of content companies generate is stored in a variety of repositories and applications across the organization. Much of the content is redundant, outdated and counterproductive, and some of it poses a compliance and legal risk for the companies. In order to alleviate this risk and efficiently manage the volumes of content, organizations need to retain only as much content as is necessary; consistently and universally apply policies on how long content should be kept; apply legal holds promptly and universally; and enable the right people with the technology needed to properly design the policies. Stellent's enterprise records and retention management solution offers a single platform that applies records policies, retention policies, legal discovery and content holds to all relevant content across an organization regardless of where it is stored and without requiring it to be moved in a consistent, legally defensible way.
- *Content Filtering and Conversion:* Stellent's content filtering and conversion technologies support multiple operating systems and international environments. These technologies enable access to content in applications for diverse markets such as content management, search and retrieval, security and policy management, mobile and wireless, messaging, collaboration and publishing.

SALES AND MARKETING

We market and sell our products using a combination of direct and indirect distribution channels primarily in North America and Europe. Our primary distribution channel is our direct sales force, which targets mid- and large-size organizations. Our sales personnel work with target accounts to address unsolved business needs which can be satisfied by the application of a business process built around our Stellent Universal Content Management software. The analysis process will typically include a business process and technical systems evaluation performed by our pre-sales personnel, followed by demonstrations of our products' capabilities and direct negotiations with our sales staff. As part of our selling model, Stellent has chosen to focus on specific vertical markets where we have developed subject matter expertise in these markets to solve common business problems. In addition, we have used internal and external telemarketing operations that are responsible for customer prospecting, lead generation and follow-up. These activities identify and develop leads for further sales efforts by our direct sales force. As of March 31, 2006, we had a worldwide total of 122 direct and indirect sales and sales support personnel and 27 marketing personnel, which includes business development and alliances.

We also use indirect sales channels to increase the distribution and visibility of our products through strategic alliances with resellers, OEMs, key systems integrators and other channel partners in both domestic and international markets.

We currently have operations or collaborations in Australia, Germany, Japan, Korea, the Netherlands, the United Kingdom and the United States. Our ability to achieve significant revenue growth in the future will depend in large part on how successfully we recruit, train and retain sufficient direct and indirect sales and support personnel, and how well we continue to establish and maintain relationships with our strategic partners, OEMs, key systems integrators and other channel partners.

We use a variety of marketing programs to build market awareness of our brand name and of our products, as well as to attract potential customers to our products. A broad mix of programs is used to

accomplish these goals, including market research, product and strategy updates with industry analysts, public relations activities, direct mail and relationship marketing programs, seminars, trade shows, speaking engagements, Web site marketing and joint marketing programs. Our marketing organization produces marketing materials in support of sales to prospective customers that include brochures, data sheets, white papers, presentations and demonstrations.

CONTRACTS

The types of license contracts we enter into with our customers are typically perpetual arrangements for our end-user customers or are term-based arrangements for our OEM customers. Virtually all of our customers initially purchase maintenance contracts, which entitle them to unspecified upgrades and product support. The primary reward or benefits to us of a perpetual licensing arrangement is the annual renewal of post-contract support. The primary benefit of a term-based license is the ability to predict future license revenue streams from that customer. The primary risk associated with the perpetual licensing arrangement is the non-renewal of post-contract support. The primary risk of a term-based license arrangement is the potential non-renewal of that arrangement. Many of our direct customers enter into services arrangements, which may include needs assessment, software integration, security analysis, application development and training. Application development generally is not critical to the functionality of the delivered software.

PRODUCT TRAINING

We provide a full range of educational courses on our Universal Content Management software. The comprehensive web-based modules and instructor-led classes enable business end-users, administrators, site designers, and developers to use our software more productively. Standard classes are scheduled at our designated worldwide training facilities, and both standard and customized classes are frequently taught at customer sites.

RESEARCH AND DEVELOPMENT

We have made substantial investments in research and development through both internal development and technology acquisitions. Our research and development expenditures for fiscal 2004, 2005 and 2006, were approximately \$13.3 million, \$18.0 million and \$20.2 million, respectively. Research and development expenses represented 18%, 17%, and 16%, respectively, of total revenue in those years. We expect that we will continue to commit significant resources to research and development in the future. As of March 31, 2006, we had 150 employees engaged in research and development activities.

In order to continue to provide product leadership in the content management and content components market, we intend to make major product releases approximately once per year. The success of new introductions is dependent on several factors, including timely completion and market introduction of new products, differentiation of new products and enhancements from those of our competitors and market acceptance of new products and enhancements.

The market for our products is characterized by rapid technological change, frequent new product introductions and enhancements, evolving industry standards and rapidly changing customer requirements. The introduction of products incorporating new technologies and the emergence of new industry standards could render existing products obsolete and unmarketable. Our future success will depend in part on our ability to anticipate changes, enhance our current products, develop and introduce new products that keep pace with technological advancements and address the increasingly sophisticated needs of our customers. We may not be successful in developing and marketing new products and enhancements that respond to competitive and technological developments and changing customer needs.

PROPRIETARY RIGHTS AND LICENSING

We rely on a combination of copyright, trade secret, trademark, confidentiality procedures and contractual provisions to protect our proprietary rights. United States and international copyright laws provide limited protections for our software, documentation and other written materials. We license our products in object code format for limited use by customers. We treat the source code for our products as a trade secret and we require all employees and third-parties who need access to the source code to sign non-disclosure agreements.

Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy aspects of our products or to obtain and use information that we regard as proprietary. Policing unauthorized use of our products is difficult, and while we are unable to determine the extent to which piracy of our software exists, software piracy can be expected to be a persistent problem. Litigation may be necessary in the future to enforce our intellectual property rights, to protect our trade secrets, to determine the validity and scope of the proprietary rights of others or to defend against claims of infringement or invalidity. However, the laws of many countries do not protect our proprietary rights to as great an extent as do the laws of the United States. Any litigation could result in substantial costs and diversion of resources and could have a material adverse effect on our business, operating results and financial condition. Our efforts to protect our proprietary rights may not be adequate or our competitors may independently develop similar technology. Our failure to meaningfully protect our property could have a material adverse effect on our business, operating results and financial condition.

Third parties may make claims of infringements with respect to our current or future product, but we cannot be sure that any such claims will arise. We expect that developers of content management and content component products will increasingly be subject to infringement claims as the number of products and competitors in our market grows and as the functionality of products in different segments of the software industry increasingly overlaps. Any claims, with or without merit, could be time consuming to defend, result in costly litigation, divert management's attention and resources, cause product shipment delays or require us to enter into royalty or licensing agreements. Royalty or licensing agreements, if required, may not be available on terms acceptable to us or at all. A successful claim of product infringement against us and our failure or inability to license the infringed technology or develop or license technology with comparable functionality could have a material adverse effect on our business, operating results and financial condition.

ACQUISITIONS

In June 2005, we acquired certain assets of privately held e-Onehundred Group, a financial compliance solutions provider, for \$5.0 million in cash, 274,000 shares of the Company's stock valued at \$2.0 million and a potential \$2.0 million cash earn-out over a one-year period based upon revenue performance. We acquired certain assets of the e-Onehundred Group to strengthen our domain expertise and to add to our product set which will enable us to more quickly capitalize on the growing financial compliance market by efficiently building a portfolio of applications on top of its scalable compliance platform.

SUPPLIERS

We have no sole source or limited source suppliers that we materially depend upon for our products described above.

COMPETITION

The market for content management and content transformation software is intensely competitive, subject to rapid technological change and significantly affected by new product introductions and

enhancements and other market activities of industry participants. We believe our competitive advantages include superior technology and lower overall cost of ownership. However, we expect competition to persist and intensify in the future. Our primary source of competition across the range of our product and service offerings is from content management products offered by companies such as EMC Corporation, FileNET Corporation, IBM Corporation, Interwoven, Inc., Microsoft Corporation, and Vignette Corporation. We also compete with current or potential customers who may develop solutions internally. Our governance, risk and compliance solutions primarily compete with specialty providers in the area, including OpenPages, Paisley Consulting, and Bwise. Our competitive advantage over these providers is the underlying ECM platform that we leverage as well as our financial viability. In the area of content filtering and conversion technologies, our primary competition is Verity, which was recently acquired by Autonomy.

Many of our competitors have longer operating histories and significantly greater financial, technical, marketing and other resources than we do and thus may be able to respond more quickly to new or changing opportunities, technologies and customer requirements. In particular, we believe that EMC Corporation, FileNet Corporation, IBM Corporation and Microsoft Corporation all have larger market positions than we do. Also, many current and potential competitors have greater name recognition and access to larger customer bases than we have. Such competitors may be able to undertake more extensive promotional activities and offer more attractive terms to purchasers than we can. In addition, current and potential competitors have established or may establish cooperative relationships among themselves or with third parties to enhance their products. Accordingly, it is possible that new competitors or alliances among competitors may emerge and rapidly acquire significant market share.

Competition in our market could materially and adversely affect our ability to obtain revenues from software license fees from new or existing customers on terms favorable to us. Further, competitive pressures may require us to reduce the price of our software. In either case, we cannot be sure that we will be able to compete successfully with existing or new competitors or that competition will not have a material adverse effect on our business, operating results and financial condition.

EMPLOYEES

As of March 31, 2006, we had 560 employees. Our future success will depend in part on our ability to attract, retain, integrate and motivate highly qualified sales, technical and management personnel, for whom competition is intense. From time to time we also employ independent contractors to support our services, product development, sales and marketing departments. Our employees are not represented by any collective bargaining unit, and we have never experienced a work stoppage. We believe our relations with our employees are good.

GEOGRAPHIC INFORMATION

Financial information about geographic areas is incorporated by reference from Footnote 11 to our Consolidated Financial Statements included elsewhere in this Annual Report on Form 10-K.

AVAILABLE INFORMATION

Our Web site is: <http://www.stellent.com>. We make available, free of charge, through our Web site, our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports, as soon as reasonably practicable after we electronically file such materials with, or furnish them to, the Securities and Exchange Commission.

Item 1A. Risk Factors

DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS

The risks and uncertainties described below are not the only risks we face. These risks include those that we consider to be significant at this time to investment decisions regarding our common stock. There may be risks that you, in particular, view differently than we do, and there are other risks and uncertainties that we do not presently know of or that we currently deem immaterial, but that may, in fact, harm our business in the future. If any of these events occur, they could have a material adverse effect on our business, results of operations and financial condition could be seriously harmed, and the trading price of our common stock could decline.

You should consider carefully the following factors, in addition to other information in this Annual Report on Form 10-K, in evaluating our company and business.

BECAUSE OUR INFRASTRUCTURE COSTS ARE GENERALLY FIXED AND THE TIMING OF OUR REVENUES FROM QUARTER TO QUARTER IS HIGHLY VARIABLE, OUR FUTURE PERFORMANCE IS DIFFICULT TO PREDICT, MAKING AN INVESTMENT IN OUR COMMON STOCK SUBJECT TO HIGH VOLATILITY.

While our products and services are not seasonal, our revenues and operating results are difficult to predict and may fluctuate significantly from quarter to quarter. If our quarterly revenues or operating results fall below the expectations of investors or securities analysts, the price of our common stock could fall substantially. A large part of our sales typically occurs in the last month of a quarter, frequently in the last week or even the last days of the quarter. If these sales were delayed from one quarter to the next for any reason, our operating results could fluctuate dramatically. In addition, our sales cycles may vary, making the timing of sales difficult to predict. Furthermore, our infrastructure costs are generally fixed. As a result, modest fluctuations in revenues between quarters may cause large fluctuations in operating results. These factors all tend to make the timing of revenues unpredictable and may lead to high period-to-period fluctuations in operating results.

Our quarterly revenues and operating results may fluctuate for several additional reasons, many of which are outside of our control, including the following:

- demand for our products and services;
- the timing of new product introductions and sales of our products and services;
- unexpected delays in introducing new products and services;
- increased expenses, whether related to sales and marketing, research and development, administration or services;
- changes in the rapidly evolving market for Web content management solutions;
- the mix of revenues from product licenses and services, as well as the mix of products licensed;
- the mix of services provided and whether services are provided by our staff or third-party contractors;
- the mix of domestic and international sales;
- costs related to possible acquisitions of technology or businesses;
- general economic conditions; and
- public announcements by our competitors.

WE HAVE A HISTORY OF MAKING ACQUISITIONS, INCLUDING LARGE STRATEGIC ACQUISITIONS, AND FUTURE POTENTIAL ACQUISITIONS MAY BE DIFFICULT TO COMPLETE OR TO INTEGRATE AND MAY DIVERT MANAGEMENT'S ATTENTION AND CAUSE OUR OPERATING RESULTS TO SUFFER.

We may seek to acquire or invest in businesses, products or technologies that are complementary to our business. If we identify an appropriate acquisition opportunity, we may be unable to negotiate favorable terms for that acquisition, successfully finance the acquisition or integrate the new business or products into our existing business and operations. In addition, the negotiation of potential acquisitions and the integration of acquired businesses or products may divert management time and resources from our existing business and operations. To finance acquisitions, we may use a substantial portion of our available cash or we may issue additional securities, which would cause dilution to our shareholders.

WE MAY NOT BE PROFITABLE IN THE FUTURE, WHICH WOULD CAUSE OUR FINANCIAL POSITION TO SUFFER AND MAY CAUSE THE MARKET PRICE OF OUR STOCK TO FALL.

Our revenues may not grow in future periods and we may not sustain profitability. If we do not sustain profitability, our financial position will suffer and the market price of our stock may fall. Our ability to sustain profitable operations depends upon many factors beyond our direct control. These factors include, but are not limited to:

- the demand for our products;